

**ASSEMBLY BILL**

**No. 26**

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**Introduced by Assembly Member Charles Calderon**

January 29, 2009

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An act to amend Sections 17282 and 24436.1 of, and to repeal Sections 17281 and 24436 of, the Revenue and Taxation Code, relating to taxation, to take effect immediately, tax levy.

LEGISLATIVE COUNSEL'S DIGEST

AB 26, as introduced, Charles Calderon. Personal and corporate income taxes: deductions: illegal activities.

The Personal Income Tax Law and the Corporation Tax Law allow various deductions in computing the income that is subject to the taxes imposed by those laws. Those laws, in modified conformity to federal income tax laws, disallow any deduction from gross income if that income is directly derived from, or directly tends to promote or further, illegal activities relating to lotteries, gaming, or horse racing, and other specified illegal activities.

This bill would instead disallow a deduction for expenses attributable to income derived by a taxpayer from any criminal activity punishable under the Penal Code, specified illegal activities relating to drug trafficking, and insurance fraud, as provided.

This bill would result in a change in state taxes for the purpose of increasing state revenues within the meaning of Section 3 of Article XIII A of the California Constitution, and thus would require for passage the approval of  $\frac{2}{3}$  of the membership of each house of the Legislature.

The California Constitution authorizes the Governor to declare a fiscal emergency and to call the Legislature into special session for that purpose. The Governor issued a proclamation declaring a fiscal

emergency, and calling a special session for this purpose, on December 19, 2008.

This bill would state that it addresses the fiscal emergency declared by the Governor by proclamation issued on December 19, 2008, pursuant to the California Constitution.

This bill would take effect immediately as a tax levy.

Vote:  $\frac{2}{3}$ . Appropriation: no. Fiscal committee: yes.

State-mandated local program: no.

*The people of the State of California do enact as follows:*

SECTION 1. Section 17281 of the Revenue and Taxation Code is repealed.

~~17281. In computing taxable income, no deductions shall be allowed to any taxpayer on any of his or her gross income directly derived from illegal activities as defined in Chapter 9 (commencing with Section 319), 10 (commencing with Section 330), or 10.5 (commencing with Section 337.1) of Title 9 of Part 1 of the Penal Code; nor shall any deductions be allowed to any taxpayer on any of his or her gross income derived from any other activities which directly tend to promote or to further, or are directly connected or associated with, those illegal activities. A prior, final determination by a court of competent jurisdiction of the state in any criminal proceeding or any proceeding in which the state, county, city and county, city, or other political subdivision was a party thereto on the merits of the legality of the activities of a taxpayer or predecessor in interest of a taxpayer shall be binding upon the Franchise Tax Board and State Board of Equalization.~~

SEC. 2. Section 17282 of the Revenue and Taxation Code is amended to read:

17282. (a) In computing taxable income, no deductions ~~(including, including deductions for cost of goods sold) sold,~~ shall be allowed to any taxpayer ~~on~~ from any of his or her gross income directly derived from illegal activities as defined in Sections 266h or 266i of, or in Chapter 4 (commencing with Section 211) of Title 8 of, Chapter 7.5 (commencing with Section 311) of Title 9 of, Chapter 8 (commencing with Section 314) of Title 9 of, or Chapter 2 (commencing with Section 459), Chapter 5 (commencing with Section 484), or Chapter 6 (commencing with Section 503) of Title 13 of, Part 1 of the Penal Code, or as defined in *any act or omission*

*punishable under the Penal Code, Chapter 6 (commencing with Section 11350) of Division 10 of the Health and Safety Code, or Article 5 (commencing with Section 750) of Chapter 1 of Part 2 of Division 1 of the Insurance Code; nor shall any deductions be allowed to any taxpayer ~~on~~ from any of his or her gross income derived from any other activities which directly tend to promote or to further, or are directly connected or associated with, those illegal activities acts or omissions.*

(b) A prior, final determination by a court of competent jurisdiction of this state in any criminal proceedings or any proceeding in which the state, county, city and county, city, or other political subdivision was a party thereto on the merits of the legality of the activities of a taxpayer, or predecessor in interest of a taxpayer, *shall be required in order for subdivision (a) to apply and* shall be binding upon the Franchise Tax Board and the State Board of Equalization.

(c) This section, *including amendments made by the act amending this subdivision*, shall be applied with respect to taxable years which have not been closed by a statute of limitations, res judicata, or otherwise.

SEC. 3. Section 24436 of the Revenue and Taxation Code is repealed.

~~24436. In computing net income, no deductions shall be allowed to any taxpayer on any of its gross income directly derived from illegal activities as defined in Chapters 9, 10 or 10.5 of Title 9 of Part 1 of the Penal Code of California; nor shall any deduction be allowed to any taxpayer on any of its gross income derived from any other activities which directly tend to promote or to further, or are directly connected or associated with, such illegal activities. A prior, final determination by a court of competent jurisdiction of this state in any criminal proceedings or any proceeding in which the state, county, city and county, city or other political subdivision was a party thereto on the merits of the legality of the activities of a taxpayer or predecessor in interest of a taxpayer shall be binding upon the Franchise Tax Board and State Board of Equalization.~~

SEC. 4. Section 24436.1 of the Revenue and Taxation Code is amended to read:

24436.1. (a) In computing net income, no deductions ~~(including, including deductions for cost of goods sold) sold~~, shall

1 be allowed to any taxpayer ~~on~~ from any of its gross income directly  
2 derived from ~~illegal activities as defined in Sections 266h or 266i~~  
3 ~~of, or in Chapter 4 (commencing with Section 211) of Title 8 of,~~  
4 ~~Chapter 7.5 (commencing with Section 311) of Title 9 of, Chapter~~  
5 ~~8 (commencing with Section 314) of Title 9 of, or Chapter 2~~  
6 ~~(commencing with Section 459), Chapter 5 (commencing with~~  
7 ~~Section 484), or Chapter 6 (commencing with Section 503) of Title~~  
8 ~~13 of, Part 1 of the Penal Code, or as defined in any act or omission~~  
9 ~~punishable under the Penal Code, Chapter 6 (commencing with~~  
10 ~~Section 11350) of Division 10 of the Health and Safety Code, or~~  
11 ~~Article 5 (commencing with Section 750) of Chapter 1 of Part 2~~  
12 ~~of Division 1 of the Insurance Code; nor shall any deductions be~~  
13 allowed to any taxpayer ~~on~~ from any of its gross income derived  
14 from any other activities which directly tend to promote or to  
15 further, or are directly connected or associated with, those ~~illegal~~  
16 ~~activities acts or omissions.~~

17 (b) A prior, final determination by a court of competent  
18 jurisdiction of this state in any criminal proceedings or any  
19 proceeding in which the state, county, city and county, city, or  
20 other political subdivision was a party thereto on the merits of the  
21 legality of the activities of a taxpayer or predecessor in interest of  
22 a taxpayer *shall be required in order for subdivision (a) to apply*  
23 *and* shall be binding upon the Franchise Tax Board and the State  
24 Board of Equalization.

25 (c) This section, *including amendments made by the act*  
26 *amending this subdivision*, shall be applied with respect to taxable  
27 years which have not been closed by a statute of limitations, res  
28 judicata, or otherwise.

29 SEC. 5. This act addresses the fiscal emergency declared by  
30 the Governor by proclamation on December 19, 2008, pursuant  
31 to subdivision (f) of Section 10 of Article IV of the California  
32 Constitution.

33 SEC. 6. This act provides for a tax levy within the meaning of  
34 Article IV of the Constitution and shall go into immediate effect.

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